Supreme Court, U.S.
FILED

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No.

In the

Supreme Court of the United States

31/32 LEXINGTON ASSOCIATES,

Petitioner,

vs.

THE TAX APPEALS TRIBUNAL OF THE STATE OF NEW YORK AND MICHAEL H. URBACH, COMMISSIONER OF TAXATION AND FINANCE OF THE STATE OF NEW YORK,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE NEW YORK SUPREME COURT, APPELLATE DIVISION, THIRD DEPARTMENT

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the imposition of real property transfer gains tax by New York State when the taxpayer does not realize an actual gain violates the Equal Protection Clause of the Fourteenth Amendment of the United States Constitution?

PARTIES

The names of all parties to the proceeding in the court whose judgment is sought to be reviewed here appear in the caption of the case.

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PETITION FOR WRIT OF CERTIORARI

OPINIONS BELOW

The opinion of the New York State Supreme Court, Appellate Division, Third Department, is officially reported as *31/32 Lexington Associates v. Tax Appeals Tribunal,* 258 A.D.2d 684, 685 N.Y.S. 2d 329 (N.Y. App. Div. 3d Dep't 1999) and appears in the Appendix hereto at A-1. The administrative decisions of the Tax Appeals Tribunal of the State of New York and of the Administrative Law Judge, which

are not officially reported, appear at A-9 and A-39. The administrative denials of the refund claims filed by Petitioner 31/32 Lexington Associates, a New York general partnership, which are not officially reported, appear at A-31 and A-35.

JURISDICTION

The judgment of the Appellate Division was entered on February 4, 1999. Petitioner's appeal as of right to the New York State Court of Appeals pursuant to N.Y. Civ. Prac. L. & R. 5601(b)(1) was dismissed by that Court *sua sponte* on May 4, 1999. The dismissal is officially reported as *31/32 Lexington Associates v. Tax Appeals Tribunal,* 93 N.Y. 2d 919, 713 N.E. 2d 418, 691 N.Y.S. 2d 383 (1999), and the order of dismissal appears at A-5. Petitioner's subsequent motion for discretionary review (leave to appeal) pursuant to N.Y. Civ. Prac. L. & R. 5602(a)(2) was denied by the New York State Court of Appeals on August 26, 1999. The denial, which is not officially reported, appears at A-7. In accordance with Rule 13.1 of this Court, this petition is filed within 90 days of the date of denial of discretionary review (leave to appeal). The jurisdiction of this Court is invoked under 28 U.S.C. §1257(a) because the judgment of the Appellate Division sought to be reviewed draws into question the validity of a statute of a State on the ground of its being repugnant to the Constitution of the United States.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

A. Constitutional Provisions

Section 1 of the Fourteenth Amendment to the United States Constitution, which contains the Equal Protection Clause, provides in part:

> No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

B. Statutory Provisions

Section 1146(c) of the Bankruptcy Code, 11 U.S.C. §1146(c), provides as follows:

> The issuance, transfer, or exchange of a security, or the making or delivery of an instrument of transfer under a plan confirmed under section 1129 of this title, may not be taxed under any law imposing a stamp or similar tax.

Section 1441(1) of the New York State Tax Law, as in effect for transfers of real property before June 15, 1996, provides as follows:

> A tax is hereby imposed on gains derived from the transfer of real property within the state. The tax shall be at the rate of ten percent of the gain.

Section 1440(3) of the New York State Tax Law provides:

> 3. "Gain" means the difference between the consideration for the transfer of real property and the original purchase price of such property, where the consideration exceeds the original purchase price.

Section 1440(1)(a) of the New York State Tax Law provides, in part:

> "Consideration" means the price paid or required to be paid for real property . . .

C. Regulations

Section 590.66 of the New York State Real Property Transfer Gains Tax regulations provides, in part:

> Q. Is a transfer pursuant to a plan under the liquidation or reorganization provisions of the Bankruptcy Code taxable?
>
> A. Yes. . . . The United States Court of Appeals for the Second Circuit held that the debtor is not exempt from liability for the tax under section 1146(c) of the Federal Bankruptcy Code, *In re: 995 Fifth Avenue Associates, L.P., Debtor*, 963 F.2nd 503 (2d Cir. 1992).

STATEMENT OF THE CASE

31/32 Lexington Associates, a New York general partnership ("Petitioner"), is seeking a refund of real property transfer gains tax imposed by New York State on a transaction on which Petitioner had no actual gain. Petitioner sold an interest in real property and took back a second mortgage. Subsequently, the purchaser went into bankruptcy. Pursuant to the bankruptcy plan of reorganization, the property was transferred to the first mortgagee. Petitioner had no gain on the transaction.

Petitioner's claim for refund of real property transfer gains tax paid by it was denied by the New York State Tax Department and New York State courts. Imposing the New York State real property transfer gains tax when no actual gain is realized violates the Equal Protection Clause of the United States Constitution.

A. Statement of Facts

Petitioner transferred an interest in 205 and 215 Lexington Avenue, New York, New York (the "Property") to 205-15 Lex Associates ("Buyer") on or about May 26, 1988. No cash was received by Petitioner at the time of the transfer. Petitioner took back Buyer's second mortgage on the Property, as security for Buyer's obligation to pay the purchase price over a five-year period. Pursuant to the applicable provisions of the New York State real property transfer gains tax, an election was made by Petitioner to pay the gains tax in installments. The scheduled payments of gains tax were made timely by Petitioner. Petitioner had acquired the Property from Lexington Associates ("Original Owner") as a condition to the transfer of the Property by Petitioner to Buyer. Philip Pilevsky, a general partner in

Petitioner, acted as nominee for Petitioner in the acquisition of the Property by Petitioner from Original Owner and in the transfer of the Property by Petitioner to Buyer.

The Transferee Questionnaire filed by Philip Pilevsky (as nominee for Petitioner) dated March 22, 1988 reported the anticipated transfer on May 26, 1988 of the Property by Original Owner to Philip Pilevsky for consideration in the amount of $45,100,000.

The Transferor Questionnaire filed by Philip Pilevsky (as nominee for Petitioner) dated April 1988 reported the anticipated transfer on May 26, 1988 of the Property by Philip Pilevsky to Buyer for consideration in the amount of $49,100,000. The Transferor Questionnaire reported gain in the amount of $3,915,000 and anticipated gains tax in the amount of $391,500.

The Supplemental Return filed by Philip Pilevsky (as nominee for Petitioner) dated April 26, 1988 reported that no cash was received upon the transfer to Buyer and made the election to pay the entire gains tax of $391,500 in installments.

Due to the decline of the real estate market, Buyer was unable to operate the Property profitably after the first three years of ownership. Buyer was unable to keep current on the first and second mortgages and the other expenses of operating the Property. On or about February 3, 1992, Buyer commenced a Chapter 11 case in the United States Bankruptcy Court for the Southern District of New York, Case No. 92 B 40718 (PBA). Buyer's payments on the second mortgage held by Petitioner ceased upon Buyer's Chapter 11 filing. The filing of the Chapter 11 petition by Buyer acted as an automatic stay against any attempt by Petitioner to collect further payments. Pursuant to the plan of reorganization in Buyer's bankruptcy case,

Petitioner realized no gain upon the sale of the Property to Buyer.

B. Prior Proceedings

On May 24, 1993, Petitioner filed with the New York State Department of Taxation and Finance (the "Tax Department") a claim for refund of the first four payments of gains tax (the "First Refund Claim").

On July 30, 1993, the Audit Division of the Tax Department (the "Audit Division") rejected the First Refund Claim. (A-31). On February 17, 1995, the Bureau of Conciliation and Mediation Services of the Tax Department (the "BCM") issued an order sustaining the Audit Division's rejection of the First Refund Claim.

On May 5, 1995, Petitioner filed a petition (DTA No. 813845) with the Division of Tax Appeals of the Tax Department, asking for a review of the rejection of the First Refund Claim by the BCM.

On May 11, 1995, Petitioner filed a claim for refund with respect to the fifth (and final) payment of gains tax (the "Second Refund Claim").

On May 24, 1995, the Audit Division denied Petitioner's Second Refund Claim. (A-35).

On July 26, 1995, the Tax Department, in its Answer to the Petition in DTA No. 813845, admitted that Petitioner had paid the gains tax which is the subject of the First Refund Claim but opposed the refund.

On August 4, 1995, Petitioner filed a petition (DTA No. 814194) seeking review of the Audit Division's denial of the Second Refund Claim.

On October 19, 1995, the Tax Department, in its Answer to the Petition in DTA No. 814194, admitted that Petitioner had paid the gains tax which is the subject of the Second Refund Claim but opposed the refund.

On November 14, 1996, the Administrative Law Judge issued a Determination denying both Petitions and sustaining the Audit Division's denial of both of Petitioner's refund claims. The Administrative Law Judge rejected the argument made by Petitioner under the Equal Protection Clause of the United States Constitution. (A-39). The Petitioner thereupon filed a timely Notice of Exception to the Administrative Law Judge's Determination, reasserting the equal protection claim. (A-51).

On August 21, 1997, the Tax Appeals Tribunal rejected the Petitioner's claim under the Equal Protection Clause and affirmed the Determination of the Administrative Law Judge for the reasons stated in said Determination. (A-9). The Petitioner thereupon filed a timely Petition under C.P.L.R. Article 78 with the New York State Supreme Court, Appellate Division, Third Department (the "Appellate Division") for judicial review of the administrative action of the Tax Department. (A-23). Petitioner alleged that the administrative action of the Tax Department violates the Equal Protection Clause of the Fourteenth Amendment of the United States Constitution.

The Decision of the Tax Appeals Tribunal included a discussion (in dicta) concerning whether Petitioner was a proper party in interest. On March 30, 1998, Petitioner and Respondents stipulated and agreed in the Appellate Division that Petitioner is the proper party in interest. (A-55).

On February 4, 1999, the Appellate Division issued a decision affirming the Decision of the Tax Appeals Tribunal and rejecting Petitioner's claim under the Equal Protection Clause. (A-1).

REASONS FOR GRANTING THE WRIT

The writ should be granted to review the decision of the New York State courts that a tax designed to tax gains from real property may be applied differently to taxpayers who are similarly situated in terms of the amount of their actual gain.

The New York State real property transfer gains tax, as in effect for transfers of real property before June 15, 1996, is equal to 10% of the "gains derived" from a transfer of real property. Tax Law Section 1441(1).

"Gain" is defined as the difference between the consideration for the transfer of real property and the original purchase price of such property. Tax Law Section 1440(3).

"Consideration" is defined as the price paid currently or required to be paid subsequently for the real property. Tax Law Section 1440(l)(a).

The gains tax is due no later than 15 days after the date of the transfer. However, if the tax due exceeds the cash portion of the consideration, the tax may be paid in installments. If the seller takes back a purchase money mortgage, the tax payments may be extended over the term of the mortgage, not to exceed 15 years. The installment payments are limited to the "total tax due" plus interest. Tax Law Section 1442(c).

There has been litigation in the bankruptcy context as to whether the New York State real property transfer gains tax is a "stamp or similar tax" (from which debtors in Chapter 11 cases are exempt under Section 1146(c) of the Bankruptcy Code) or a tax in the nature of an income tax (which does not come within the Section 1146(c) exemption). In the case of *In re Jacoby-Bender, Inc., Debtor*, 40 B.R. 10 (1984), the

United States Bankruptcy Court for the Eastern District of New York held that the real property transfer gains tax, unlike the New York City and New York State real estate transfer taxes, is not similar to a "stamp tax" and does not come within the exemption provided by Bankruptcy Code Section 1146(c). The court based its conclusion upon the fact that the real property transfer gains tax (unlike the State and City real estate transfer taxes) is not a tax upon the real property transfer itself or upon the instrument of transfer, but is, rather, a tax upon the "gain realized by the transferor upon the transfer." 40 B.R. at 15.

The United States Court of Appeals for the Second Circuit has held that the New York State real property transfer gains tax is not a "stamp tax or a similar tax," but is, rather, a tax imposed on economic gain. *In Re 995 Fifth Avenue Associates, L.P., Debtor*, 963 F.2d 503 (2d Cir. 1992), *cert. denied*, 506 U.S. 947, 113 S.Ct. 395, 121 L.Ed.2d 302. The Second Circuit stated:

> First, and most important, New York gains tax liability is always contingent on the profitability of the underlying transaction. If the transaction yields no gain, there is no tax due. 963 F.2d at 513.

The New York State Department of Taxation and Finance has adopted the rule of the *995 Fifth Avenue Associates* decision in its own regulations. *See* Reg. Section 590.66, citing *995 Fifth Avenue Associates*.

The New York State real property transfer gains tax thus is an income tax imposed on actual *gain derived* from the transfer of real property. The name of the tax — Real Property Transfer Gains Tax — similarly makes clear that it is a tax imposed on *gains*. It is not a transfer tax or a deed tax, which, unlike a gains tax, are based on the amount of stated consideration. The amount of taxable gain is determined by comparing the

consideration received for the property with the original purchase price paid for the property. Tax Law Section 1440(3). The term "consideration" means the price paid currently or to be paid subsequently for the property. Tax Law Section 1440(1)(a). Installment payments of gains tax are permitted when a seller takes back a purchase money mortgage, so that funds will be available to pay the tax. The installment payments are not to exceed the "total tax due." Tax Law Section 1442(c). The contemplation of the statute is that a seller who is paid in installments will in fact be paid and will be taxed accordingly on his "gain derived" from the sale.

Petitioner held a second mortgage on the Property from Buyer. Buyer went into bankruptcy. Pursuant to the confirmed plan of bankruptcy reorganization, the Property was transferred to the holder of the first mortgage. As the result of Buyer's bankruptcy, Petitioner did not realize any gain on the Property. Since the gains tax is imposed only upon actual gain, the tax should be zero.

As an administrative matter, there would be no difficulty in making an initial computation of gains tax liability based on consideration stated at the time of the transfer, including the amount of mortgage indebtedness, while at the same time allowing a refund of gains tax in the event of default on a purchase money mortgage. Such an approach is consistent with the statute and regulations. It is only the Tax Department's arbitrary administrative policy, as approved by the New York State courts, which has prevented justice in Petitioner's case and denied him the equality with those similarly situated required by the Equal Protection Clause of the United States Constitution.

The gains tax statute is not constitutionally defective on its face. It is constitutionally defective, however, as applied to Petitioner, if it is interpreted to require payment of tax even though there is no actual gain realized. If a tax which is designed to tax income or gain is applied to impose unequal burdens on two taxpayers each of whom does not realize a gain, or each of whom realizes the same gain, the equal protection defect is apparent.

The equal protection defect in the Tax Department's application of the gains tax statute to Petitioner is shown by the following illustration: Taxpayer A purchases real property X for $1,000,000. Taxpayer B purchases real property Y for $1,000,000. Taxpayer A sells real property X to purchaser M for $2,000,000 cash. Taxpayer B sells real property Y to purchaser N for $2,000,000 cash and N's purchase money second mortgage in the amount of $100,000. Purchaser N goes into bankruptcy and Taxpayer B is never paid on his second mortgage from purchaser N. Taxpayer A and Taxpayer B each have received $2,000,000 cash from their transactions. Taxpayer A and Taxpayer B each have realized an economic gain of $1,000,000. Taxpayer A and Taxpayer B thus are similarly situated in terms of actual gain. However, under the gains tax as applied to Petitioner by the Tax Department, Taxpayer A is taxed on a gain of $1,000,000, while Taxpayer B (analagous to Petitioner) is taxed on a gain of $1,100,000. The difference in tax is $10,000 (10% of Taxpayer B's nonexistent additional $100,000 "gain," which Taxpayer B did not realize due to purhaser N's failure to pay the purchase money mortgage). This interpretation of the statute, which treats similarly situated taxpayers differently, is prohibited by the Equal Protection Clause.

The Appellate Division rejected the Petitioner's equal protection claim as follows:

> Because the statutory scheme here imposes a tax in all cases based upon the gain at the time of transfer, it cannot be said that petitioner's equal protection rights have been violated.

The Appellate Division's analysis of the equal protection issue is incorrect, however, as shown by the following addition to the above illustration: Taxpayer C purchases real property Z for $1,000,000. Taxpayer C sells real property Z to Purchaser O for $2,000,000 cash and O's purchase money second mortgage in the amount of $100,000. O pays the second mortgage in full. Thus, Taxpayer C has realized an economic gain of $1,100,000. Taxpayer C is *not* similarly situated economically to Taxpayer A or Taxpayer B. Taxpayer C's actual gain is $100,000 more than either Taxpayer A or Taxpayer B.

The Appellate Division sets up an equal protection class consisting of Taxpayer C and Taxpayer B (analogous to Petitioner) and concludes that no equal protection defect results when Taxpayer B is taxed in the same manner as Taxpayer C. In fact, Taxpayer C and Taxpayer B are *differently* situated: Taxpayer C's actual gain is $100,000 greater than Taxpayer B's. The Equal Protection Clause does not require that persons who are differently situated be treated differently; it requires that persons who are similarly situated be treated similarly. The equal protection defect occurs when Taxpayer A and Taxpayer B, who are in fact similarly situated in the only meaningful sense (each has an economic gain of $1,000,000) are taxed differently: Taxpayer A is taxed on a gain of $1,000,000, while Taxpayer B (analogous to Petitioner) is taxed on a gain of $1,100,000.

The Appellate Division's decision on the equal protection issue is based upon a class of taxpayers who are similarly situated only with respect to the amount of consideration stated at the time of the transfer. New York State real property transfer gains tax, however, unlike the State and City real estate transfer taxes, is not a tax upon the instrument of transfer. The gains tax is an income tax. It is a tax upon the "gain realized by the transferor upon the transfer." *Jacoby-Bender, supra*; *995 Fifth Avenue Associates, supra*; Reg. Section 590.66. The failure of the Appellate Division to consider the correct class of taxpayers in the equal protection analysis leads to the wrong equal protection conclusion. When the correct class of taxpayers is considered — those taxpayers whose actual gain is the same — the equal protection defect in the gains tax statute as applied by the Tax Department to Petitioner is apparent.

In *Stewart Dry Goods Co. v. Lewis*, 294 U.S. 550, 55 S.Ct. 525, 79 L.Ed. 1054 (1935), the United States Supreme Court invalidated a Kentucky graduated gross receipts tax imposed on the sale of retail merchandise because the rate of tax increased as the total gross receipts increased. The statute taxed similar transactions differently, depending on the amount of receipts obtained from previous transactions. The only conceivable justification for this different treatment was that a merchant's net income and consequently his ability to pay the tax increased as his volume of sales increased. The Court held this was not a rational basis for the tax because the gross receipts tax was imposed regardless of whether a merchant made a profit. *Stewart Dry Goods* stands for the proposition that gross receipts taxes that treat similarly situated taxpayers differently based on sales volume violate the Equal Protection Clause because they are imposed without regard to profits actually realized. The Court stated: "A tax upon gross receipts affects each transaction in proportion to its magnitude and irrespective of whether it is profitable or otherwise . . . A tax upon the net profits has not the

same deterrent effect, since it does not arise at all unless a gain is shown over and above expenses and losses, and the tax cannot be heavy unless the profits are large." 294 U.S. 550, 558; 55 S.Ct. 525, 529.

In *Trump v. Chu*, 65 NY2d 20, 489 NYS2d 455 (1985), *appeal dismissed* 474 US 915, Donald Trump sought a declaratory judgment that the gains tax is unconstitutional in excluding transactions where the consideration is less than $1,000,000. Mr. Trump attacked the gains tax as an unlawful gross receipts tax, citing *Stewart Dry Goods*. The New York State Court of Appeals in *Trump v. Chu* distinguished *Stewart Dry Goods* because, although liability for gains tax is triggered by gross consideration of $1,000,000 or more, "the actual calculation of the tax due depends entirely on the gain realized from the real property transfer" and "the tax will be imposed only in the case of a net profit." 489 NYS2d 455, 459. The New York State Court of Appeals upheld the $1,000,000 gains tax threshold on the ground that the gains tax *taxes only net gains*. However, the gains tax as applied by the Tax Department to Petitioner would tax his transaction even though no gain is in fact realized. This application of the statute would make the gains tax similar to the unlawful gross receipts tax prohibited by *Stewart Dry Goods*. The tax is imposed on Petitioner by the Tax Department on the amount of stated consideration, regardless of the fact that the purchase money second mortgage was not paid. Petitioner is taxed on a "gain" when he receives no actual gain; a similarly situated taxpayer who sells property for no actual gain is not taxed. The guidelines provided by the United States Supreme Court in *Stewart Dry Goods* and by the New York State Court of Appeals in *Trump v. Chu* require New York State to tax only actual gains and to allow a refund upon default in a purchase money mortgage. Otherwise, the application of the gains tax statute to Petitioner violates the Equal Protection Clause.

The gains tax statute should be applied in a manner that does not result in constitutional defects. When a statute is not constitutionally defective on its face, but is constitutionally defective under one manner of application and not constitutionally defective under a reasonable alternative manner of application, the constitutionally permissible manner of application must be followed. The reading of the statute advanced by the Petitioner is that gains tax liability should be initially fixed at the time of the transaction but subsequently adjusted upon a showing of default by the purchaser on a purchase money mortgage. This reading of the statute can be applied without administrative difficulty. It is the controlling interpretation, when the contrary interpretation results in constitutionally prohibited differences in taxation of persons who are economically similarly situated.

CONCLUSION

For all the foregoing reasons, a writ of certiorari should be issued to review the opinion and judgment of the Appellate Division.

Respectfully submitted,

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November 11, 1999

APPENDIX

SUPREME COURT – APPELLATE DIVISION

THIRD DEPARTMENT

In the Matter of
31/32 LEXINGTON ASSOCIATES,

Petitioner,

v.

TAX APPEALS TRIBUNAL OF
THE STATE OF NEW YORK et al.,

Respondents.

81231

Memorandum and Judgment

Decided and Entered: February 4, 1999

Calendar Date: December 16, 1998

Before: Mikoll, J. P., Crew III, Yesawich Jr., Spain and Carpinello, JJ.

Robinson, Brog, Leinwand, Greene, Genovese & Gluck P.C. (Babcock Maclean of counsel), New York City, for petitioner.

Eliot Spitzer, Attorney-General (Julie S. Mereson of counsel), Albany, for Michael H. Urbach, respondent.

Yesawich Jr., J.

Proceeding pursuant to CPLR article 78 (initiated in this court pursuant to Tax Law § 2016) to review a determination of respondent Tax Appeals Tribunal which sustained a real property transfer gains tax assessment imposed under Tax Law former article 31-B.

In May 1988, petitioner transferred its interest in real property located in New York City to 205-215 Lex Associates (hereinafter the buyer) for $49,100,000. The transaction was accomplished by the issuance of two purchase money mortgages. The second purchase money mortgage, which was taken back by petitioner, was to be paid in installments over a five-year period. Petitioner's net gain on the transfer was $3,910,000 and, pursuant to Tax Law former § 1441, petitioner's real property transfer gains tax liability was $391,000 or 10% of the net gain; petitioner assertedly timely paid this tax in five annual installments.

Thereafter, the buyer, without having made a single payment to petitioner, filed for chapter 11 bankruptcy. Pursuant to the approved bankruptcy plan, the property was reconveyed to the first-purchase-money-mortgage holder. Under the plan, petitioner received only $200,000 for its second purchase money mortgage, which was discharged in favor of the first mortgage holder. In due course, petitioner filed two claims seeking refunds of the real property transfer gains tax petitioner had paid. It is petitioner's contention that because there was no actual gain on the transfer of the real property, no tax liability was incurred. Petitioner's claims having been denied by respondent Division of Taxation and Finance, the Administrative Law Judge and respondent Tax Appeals Tribunal, petitioner appeals.

We find unconvincing petitioner's underlying premise that for real property transfer gains tax liability to attach to a real estate transaction, a gain must have been actually realized. It has been held repeatedly that an event which occurs subsequent to the transfer of real property does not

impact upon the amount of tax owed, for the gain is calculated based upon the consideration paid or owing on the date of the transfer of the title (*see, Matter of Brockman v Tax Appeals Tribunal of State of N.Y.*, 238 AD2d 693, 694; *see, e.g., Matter of South Suffolk Recreation Ventures v. Tax Appeals Tribunal of State of N.Y.*, 224 AD2d 874, 875, *lv denied*, 88 NY2d 803; *Matter of Wanat v Tax Appeals Tribunal of State of N.Y.*, 224 AD2d 873, 874, *lv denied* 88 NY2d 803). Consideration in this context includes the face value of a purchase money mortgage assumed or given for the sale and transfer of the property (*see*, Tax Law former § 1440 [1] [a]; *see also, Matter of Fazkap Assocs. v Commissioner of N.Y. State Dept. of Taxation & Fin.*, 232 AD2d 747, 748). In view of these settled principles, the decision to deny petitioner's refund requests was neither arbitrary nor capricious.

The only other of petitioner's arguments meriting comment is its contention that the tax as applied violates the State or Federal Equal Protection Clauses. Initially, we note that petitioner's reliance upon *Stewart Dry Goods Co. v Lewis* (294 US 550) is misplaced, for the tax at issue in the instant case is measured by the gain at the time of transfer and not, as in *Stewart Dry Goods Co. v Lewis* (*supra*), on gross receipts, regardless of the net profit earned. Thus, the fact that petitioner did not collect this gain because it, for its own reasons, elected to take back an unsecured second purchase money mortgage is of no moment.

Moreover, a statute "must be upheld if the challenged 'classification is rationally related to achievement of a legitimate state purpose'" (*Matter of Union Carbide Chems. & Plastic Co. v. Tax Appeals Tribunal of State of N.Y.*, 213 AD2d 807, 809, *appeal dismissed* 85 NY2d 1031, *lv denied* 86 NY2d 710, quoting *Western & S. Life Ins. Co. v Board of Equalization of Cal.*, 451 US 648, 657). The burden is upon the taxpayer to demonstrate that the statue distinguishes among taxpayers in a manner that was "'palpably arbitrary' or tantamount to 'invidious discrimination'" (*Matter of Capital Fin. Corp v Commissioner of Taxation & Fin.*, 218

AD2d 230, 233, quoting *Trump v Chu*, 65 NY2d 20, 25, *appeal dismissed* 474 US 915). Because the statutory scheme here imposes a tax in all cases based upon the gain at the time of transfer, it cannot be said that petitioner's equal protection rights have been violated (*see*, *Matter of Brockman v. Tax Appeals Tribunal of State of N.Y.*, *supra*, at 695).

Mikoll, J.P., Crew III, Spain and Carpinello, JJ., concur.

ADJUDGED that the determination is confirmed, without costs, and petition dismissed.

Enter:

/s/ Michael J. Novack

Michael J. Novack
Clerk of the Court

STATE OF NEW YORK,
COURT OF APPEALS

In the Matter of
31/32 Lexington Associates,

Appellant,

Mo. No. 429

SSD 19

v.

Tax Appeals Tribunal of the State
of New York et al.,

Respondents.

At a session of the Court, held at Court of Appeals Hall in the City of Albany on the fourth day of May 1999

Present, HON. JUDITH S. KAYE,
Chief Judge, presiding.

The appellant having filed notice of appeal in the above title and due consideration having been thereupon had, it is

ORDERED, that the appeal be and the same hereby is dismissed without costs, by the Court *sua sponte*, upon the ground that no substantial constitutional question is directly involved.

/s/ Stuart M. Cohen

Stuart M. Cohen
Clerk of the Court

STATE OF NEW YORK,
COURT OF APPEALS

In the Matter of
31/32 Lexington Associates,

Appellant,

Mo. No. 429

SSD 19

v.

Tax Appeals Tribunal of the State
of New York et al.,

Respondents.

DECISION May 4, 1999

Appeal dismissed without costs, by the Court *sua sponte*, upon the ground that no substantial constitutional question is directly involved.

STATE OF NEW YORK,
COURT OF APPEALS

In the Matter of
31/32 Lexington Associates,

Appellant, **3-10**

v. **Mo. No. 703**

Tax Appeals Tribunal of the State
of New York et al.,

Respondents.

At a session of the Court, held at Court of Appeals Hall in the City of Albany on the twenty-sixth day of August 1999

Present, HON. JUDITH S. KAYE,
Chief Judge, presiding.

A motion for leave to appeal to the Court of Appeals in the above cause having heretofore been made upon the part of the appellant herein and papers having been submitted thereon and due deliberation having been thereupon had, it is

ORDERED, that the said motion be and the same hereby is denied with one hundred dollars costs and necessary reproduction disbursements.

/s/ Stuart M. Cohen

Stuart M. Cohen
Clerk of the Court

STATE OF NEW YORK,
COURT OF APPEALS

In the Matter of
31/32 Lexington Associates,

Appellant,

3-10

Mo. No. 703

v.

Tax Appeals Tribunal of the State
of New York et al.,

Respondents.

DECISION August 26, 1999

Motion for leave to appeal denied with one hundred dollars costs and necessary reproduction disbursements.

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petitions

of

31/32 LEXINGTON ASSOCIATES

for Revision of a Determination or for Refund of Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law.

DECISION

DTA NOS. 813845

AND 814194

Petitioner 31/32 Lexington Associates, c/o Philips International, 417 Fifth Avenue, New York, New York 10016, filed an exception to the determination of the Administrative Law Judge issued on November 14, 1996. Petitioner appeared by Robinson Brog Leinwand Greene Genovese & Gluck, P.C. (Babcock MacLean, Esq., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Herbert M. Friedman, Jr., Esq., of counsel).

Petitioner filed a brief and reply brief in support of its exception. The Division of Taxation filed a brief in opposition. Petitioner's request for oral argument was denied.

After reviewing the entire record in this matter, the Tax Appeals Tribunal renders the following decision.

Issues

I. Whether the Division of Taxation, in calculating consideration for the transfer of a certain interest in real property, properly included the face value of a purchase money mortgage despite its subsequent devaluation, so that the Division of Taxation's denial of petitioner's refund claims was justified.

II. Whether the imposition of gains tax in this matter violates petitioner's rights under the Equal Protection Clause of the United States Constitution.

Findings of Fact

We find the facts as determined by the Administrative Law Judge, except for findings of fact "1" through "7" which have been modified. We have also made an additional finding of fact. The Administrative Law Judge's findings of fact, the modified findings of fact and the additional finding of fact are set forth below.

We modify findings of fact "1," "2" and "3" of the Administrative Law Judge's determination to read as follows:

> The record on submission is extremely bare. It does not include a copy of a transferor questionnaire filed by 31/32 Lexington Associates to report its anticipated transfer of the property at issue, 205-215 Lexington Avenue in New York City ("Manhattan property"). Rather, Exhibit "M" of the Division of Taxation ("Division") is a photocopy of a transferee questionnaire filed by Philip Pilevsky, as transferee, c/o Philips International,[1] dated March 22, 1988. This

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[1] Petitioner's address shown at the beginning of this decision is also in care of Philips International.

questionnaire was filed and signed by Mr. Pilevsky in an individual capacity. This transferee questionnaire reported the anticipated transfer on May 26, 1988 of the Manhattan property by a transferor identified as Lexington Associates for consideration to be paid by Philip Pilevsky of $45,100,000.00.[2] Mr. Pilevsky reported that the type of interest to be acquired from Lexington Associates in the Manhattan property was (i) a fee interest and (ii) a leasehold assignment or surrender.

The Division's Exhibit "L" is a photocopy of a transferor questionnaire also filed by Philip Pilevsky, as transferor, c/o Philips International, dated April 1988 (without a specific day designated). This questionnaire was filed by Mr. Pilevsky in an individual capacity. This transferor questionnaire reported the anticipated transfer on May 26, 1988 of the Manhattan property to a transferee identified as 205-15 Lex Associates. Mr. Pilevsky reported that the type of interest to be transferred in the Manhattan property was a "contract assignment." Consequently, it appears that Mr. Pilevsky assigned his contract to purchase the Manhattan property from Lexington Associates over to an entity known as 205-15 Lex Associates.

Petitioner's Exhibit "1" is a short affidavit dated March 28, 1996 of David Werner, who described himself as "a general partner" in petitioner. According to Mr. Werner, petitioner "transferred an interest in 205 and 215 Lexington Avenue . . . to 205-15 Lex Associates . . . on or about May 26, 1988."

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[2] The Administrative Law Judge found, *inter alia*, that Mr. Pilevsky apparently purchased the Manhattan property from petitioner. He also found that the property was being transferred by a transferor identified as Lexington Associates, *presumably* 31/32 Lexington Associates. These findings are deleted, since there is nothing in the record to support them.

Mr. Werner provided no facts that would establish a relationship between Mr. Pilevsky and petitioner or Mr. Pilevsky and himself. Mr. Werner provided no details to show how petitioner came to own the subject property, and he did not provide any details concerning Mr. Pilevsky's assignment of his contract rights to purchase the property from Lexington Associates to the entity described as 205-15 Lex Associates. There is no evidence that Philip Pilevsky had an ownership interest in petitioner or was authorized to act on its behalf. If Mr. Pilevsky was associated with petitioner, there is no explanation for his failure to submit an affidavit showing that fact. There is nothing in the record to show a relationship between Lexington Associates and 31/32 Lexington Associates or to show whether or not they are the same entity. Other than as a mailing address, there is no information whatever about Philips International. In brief, the facts concerning petitioner's involvement with this real estate transaction have not been made part of the record.[3]

We modify finding of fact "4" of the Administrative Law Judge's determination to read as follows:

> The transferee questionnaire filed by Philip Pilevsky (Division's Exhibit "M") shows consideration to be paid to Lexington Associates by Mr. Pilevsky of $45,100,000.00 In addition, Mr. Pilevsky reported brokerage fees to be paid by him to a real estate broker of $450,000.00. In comparison, the transferor questionnaire filed by Philip Pilevsky (Division's Exhibit "L") shows consideration to be paid to Mr. Pilevsky by 205-15 Lex Associates, c/o Arnold Schotsky, Esq., of the Long Island law firm of

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[3] We modified these findings of fact to more accurately reflect the record.

Gandin, Schotsky & Rappaport, of $49,100,000.00. Mr. Pilevsky reported a gain subject to tax of $3,915,000.00 after deducting original purchase price of $45,185,000.00 calculated as follows:

Purchase price paid to acquire real property	$45,100,000.00
Legal expenses to acquire property	45,000.00
Legal expenses to sell property	40,000.00
Original purchase price	$45,185,000.00

Consideration to be received by Mr. Pilevsky from 205-15 Lex Associates of $49,100,000.00 less original purchase price of $45,185,000.00 equals a gain subject to real property transfer gains tax of $3,915,000.00, with anticipated tax due of $391,500.00 (10% of $3,915,000.00).[4]

We modify finding of fact "5" of the Administrative Law Judge's determination to read as follows:

The Division also submitted for review a photocopy of a supplemental return dated April 26, 1988 filed by Mr. Pilevsky, in his individual capacity, as transferor of the property at issue to 205-15 Lex Associates (Division's Exhibit "P"). By this Supplemental Return, Mr. Pilevsky chose to defer his payment of the gains tax due. He elected to pay the tax in equal installments payable on the anniversary date of the transfer for the length of the term of a

[4] We modified the first sentence of this finding of fact to properly reflect that the consideration was to be paid to Lexington Associates and not to petitioner. We modified the last sentence of this finding of fact to clarify that Mr. Pilevsky received the consideration from 205-15 Lex Associates.

certain purchase money mortgage, which was apparently used to finance the transaction at issue. However, a copy of the purchase money mortgage was not made part of the record. Nowhere in this Supplemental Return filed by Mr. Pilevsky does it mention 31/32 Lexington Associates.[5]

We modify finding of fact "6" of the Administrative Law Judge's determination to read as follows:

> The Division's Exhibit "D" is a claim for refund of gains tax paid of $313,200.00 dated May 24, 1993, which was filed by David Werner in his capacity as partner of an entity described as 31/32 Lex Associates, a New York partnership." It appears that "Lex" was used erroneously instead of "Lexington" in the description of the entity seeking the refund claim. This refund claim is the first document filed by petitioner, and placed in evidence, to make reference to 31/32 Lexington (or Lex) Associates. This refund claim noted the following minimal facts:
>
> > "Seller transferred an interest in [the Manhattan property] to Buyer on or about May 26, 1988.
> >
> > "No cash was received by Seller at the time of the transfer. Seller took back Buyer's second mortgage on the Property, as security for Buyer's obligation to pay the purchase price over a five-year period. Pursuant to the applicable provisions of the New York State real property gains tax, an election was made by Seller to pay the gains tax in installments. The scheduled payments of gains tax were made timely by Seller."

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[5] We modified this finding of fact to more accurately reflect the record.

We note that this refund claim contradicts the other evidence in the record (transferor questionnaire, Tentative Assessment and Return and Supplemental Return filed with the Division by Mr. Pilevsky), since it asserts: i) that petitioner, and not Philip Pilevsky, was the seller of the Manhattan property; and ii) that it, and not Mr. Pilevsky, paid the gains tax here. No contracts, cancelled checks or closing documents were offered in evidence to support petitioner's refund claim.[6]

We modify finding of fact "7" of the Administrative Law Judge's determination to read as follows:

This refund claim dated May 24, 1993 shows tax installments paid on May 17, 1989, May 2, 1990, May 20, 1991 and May 27, 1992, which totaled $313,200.00. Petitioner's second refund claim dated May 11, 1995 (Division's Exhibit "I") seeks a refund of a fifth installment payment made on May 26, 1993 of $78,300.00. The two refund claims total $391,500.00, which corresponds to the amount of gains tax reported due by Mr. Pilevsky on his transfer of the Manhattan property to 205-15 Lex Associates. There is nothing in the record to show that petitioner, rather than Mr. Pilevsky, paid the gains tax here. Neither Mr. Werner's affidavit nor the refund applications themselves show a business or other connection between Mr. Pilevsky and petitioner. There is no documentation in the record to show an acquisition or transfer of the Manhattan property by an entity known as 31/32 Lexington Associates.[7]

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[6] We modified this finding of fact to more accurately reflect the record.

[7] We modified this finding of fact to more accurately reflect the record.

Pursuant to an order of the United States Bankruptcy Court dated June 22, 1993 (petitioner's Exhibit "3"), the reorganization of 205-15 Lex Associates under Chapter 11 of the Bankruptcy Code was confirmed. Under the reorganization plan (petitioner's Exhibit "2"), petitioner released and discharged a "Second Mortgagee Claim" against 205-15 Lex Associates in exchange for a payment of $200,000.00. In addition, the Manhattan property was reconveyed to an entity known as 205/215 Lexington Limited Partnership, which apparently was the first mortgagee on the Manhattan property.

In its refund claims, petitioner asserts that it "will realize no gain upon the sale of the Property to Buyer" because of the bankruptcy 205-15 Lex Associates. However, the record does not, in fact, disclose the total payments made by 205-15 Lex Associates to Mr. Pilevsky or to petitioner.

By a letter dated July 30, 1993 (Division's Exhibit "E"), petitioner's refund claim dated May 25, 1993 in the amount of $313,200.00 was denied because "[t]he tax was properly calculated on *the date of transfer*" (emphasis in original). By a letter dated May 24, 1995 (Division's Exhibit "J"), petitioner's refund claim dated May 12, 1995 in the amount of $78,300.00 was also denied for the same reason.

We make the following additional finding of fact:

> The transferor questionnaire, the transferee questionnaire, the Tentative Assessment and Return and the Supplemental Return filed by Mr. Pilevsky regarding the transfer of the Manhattan property never make any reference to 31/32 Lexington Associates. The first time the name 31/32 Lexington Associates appears is in the refund applications. No deed, contract or contract assignments, closing documents or other source documentation were placed in evidence to show the parties and interests in the subject transaction. None of the documents Mr. Pilevsky filed with the Division purport to show that

he is filing in a representative capacity on behalf of an entity.

The Determination of the Administrative Law Judge

The Administrative Law Judge rejected petitioner's claim that gains tax may be imposed only in the case of an actual gain. Rather, the Administrative Law Judge noted that gains tax has been imposed in situations of speculative profit and in situations where real estate transactions have soured. The Administrative Law Judge noted that in *Matter of Brockman* (Tax Appeals Tribunal, April 4, 1996, *confirmed Matter of Brockman v. Tax Appeals Tribunal*, ___AD2d___, 656 NYS2d 429) the major portion of the sales price was financed by a purchase money note and mortgage from the buyer in the amount of $8,500,000.00. The buyer never made any payments on this note. Like petitioner, the Brockmans argued that because they suffered a loss, the imposition of gains tax was not rational and violated their equal protection rights. The Administrative Law Judge noted that we denied the Brockmans' claims for refund of gains tax and held them liable for gains tax.

The Administrative Law Judge pointed out that in *Brockman* we emphasized that subsequent events do not alter the value that the consideration had *at the time of the transfer*, citing our decision in *Matter of Starburst Dev. Co.* (Tax Appeals Tribunal, May 5, 1994) where we stated:

> "the moment that the taxable event occurs, i.e., the transfer of the real property, is the temporal restriction underlying the entire gains tax. Consistent with this interpretation, we have held that the consideration for the transfer is fixed at this moment and is not reduced by subsequent events . . . . To deviate from this theory, as petitioner suggests, and exclude transactions from the definition of transfer of real property based on subsequent events would, in our view, be contrary to the entire scheme of the tax."

The Administrative Law Judge also recognized that in *Brockman* we noted that our conclusion that the amount of gains tax due is to be finally determined by the amount of consideration paid or required to be paid on the date of the transfer had been affirmed on appeal (see, *Matter of Wanat v. Tax Appeals Tribunal*, 224 AD2d 873, 638 NYS2d 251, *lv denied* 88 NY2d 803, 645 NYS2d 446, *confirming Matter of Wanat*, Tax Appeals Tribunal, September 15, 1994; *Matter of South Suffolk Recreation Ventures v. Tax Appeals Tribunal*, 224 AD2d 874, 638 NYS2d 515, *lv denied* 88 NY2d 803, 645 NYS2d 446, *confirming Matter of South Suffolk Recreation Ventures*, Tax Appeals Tribunal, November 3, 1994). In *Wanat*, which the Administrative Law Judge viewed as on point, we held that the amount of the consideration calculated at the time of the transfer is not affected by the transferee's later default on a note and mortgage.

The Administrative Law Judge rejected petitioner's contention that the amendment of the gains tax law in 1993 (L 1993, ch 57, § 60), which deemed "consideration" to be limited to the fair market value of the property transferred to a lender in foreclosure proceedings, means that gains tax may be imposed only on an actual gain. The Administrative Law Judge also pointed out that this amendment only applies to transactions occurring on or after April 15, 1993 (L 1993, ch 57, § 418[8]).

The Administrative Law Judge further concluded that the Legislature has manifested no intent to ignore a transaction for purposes of gains tax due to events occurring subsequent to the time of transfer.

The Administrative Law Judge agreed with petitioner that the real property transfer gains tax is not viewed as a stamp tax, but rather as a tax on income in the context of bankruptcy litigation (*see, In re 995 Fifth Ave. Assocs., L.P.*, 963 F2d 503, *cert denied* 506 US 947, 121 L Ed 2d 302). However, the Administrative Law Judge concluded that the fact that gains tax due is calculated at the time of transfer and

may not be reduced by subsequent events does not mean that it is not a tax on or measured by income or gross receipts (*see, Matter of Brockman, supra*).

Finally, the Administrative Law Judge rejected petitioner's argument that its right to equal protection of the law is violated by holding it liable for gains tax on a transaction that later soured, citing our decision in *Matter of Brockman* (*supra*) where we stated:

> "Neither the Federal nor the State constitution required that all taxpayers be treated identically; they only require that those similarly situated be treated uniformly (*see, Matter of Foss v. City of Rochester*, 65 NY2d 247, 491 NYS2d 128; *Matter of Executive Land Corp. v. Chu*, 150 AD2d 7, 545 NYS2d 354). Requiring petitioners to pay the gains tax does not violate their constitutional rights because petitioners are being treated the same as all other similarly situated taxpayers – they are required to calculate the tax based upon the value of the consideration at the time of the transfer (*see, Matter of Rapoport*, Tax Appeals Tribunal, August 31, 1995.)"

Arguments on Exception

Petitioner makes the same arguments as it did below.

Petitioner claims that denying its refund claims is contrary to the Tax Law and to basic principles of fairness and common sense. According to petitioner, the gains tax is imposed only on "actual economic gain." It supports this statement by citing to litigation in the bankruptcy context where the gains tax has been viewed not as a stamp tax, but rather as an income tax or a tax imposed on economic gain. Petitioner states it had no gain because the purchaser went bankrupt.

Petitioner also argues that the amendment of the gains tax law in 1993 limits the calculation of "consideration" to the fair market value of the property transferred to a lender in foreclosure proceedings or a transfer in lieu of foreclosure. Further, petitioner maintains that to tax a real estate transaction even where gain is not derived would be defective under the Equal Protection Clause.

Petitioner argues that none of the cases relied upon by the Division address its central argument that when the correct class of similarly situated taxpayers is identified, i.e., taxpayers in petitioner's position, the gains tax statute as applied to petitioner violates the Equal Protection Clause (Petitioner's reply brief, p. 2).

The Division counters, citing to our earlier decisions, that in computing consideration the face amount of a mortgage at the time of transfer is properly used (*Matter of Normandy Assocs.*, Tax Appeals Tribunal, March 23, 1989). Subsequent events, the Division argues, which may effect the transferor's actual gain are irrelevant. The Division also points out that we rejected an equal protection argument similar to petitioner's in *Matter of Rapoport* (*supra*).

Opinion

We affirm the determination of the Administrative Law Judge.

While we agree with the above conclusions of the Administrative Law Judge, we would dismiss the petition on jurisdictional grounds. Although not raised by either party before the Administrative Law Judge, a jurisdictional issue may be raised at any time and cannot be waived (*United States v. Wright*, 658 F Supp 1, 86-1 USTC ¶ 9457). As stated above, this record is very minimal. Tax Law former § 1445(1) provided, in pertinent part, that "[a] transferor *claiming to have* erroneously *paid* the [gains] tax . . . may file an application for a refund" (emphasis added). If 31/32 Lexington Associates was ever a party to the subject

transaction or had an ownership interest in the Manhattan property, or ever transferred the Manhattan property or ever paid gains tax on such transfer, petitioner has not demonstrated it. The evidence is, at best, contradictory. The bankruptcy papers suggest that petitioner held a second mortgage on the subject property and that such mortgage was forgiven in return for $200,000.00. That fact, by itself, does not tell us anything about the subject transaction. The note and mortgage is not part of the record. We cannot assume that because petitioner held a second mortgage on the subject property that that mortgage arose from the subject transaction. Further, there is nothing in this record to show that petitioner paid any gains tax. Without evidence of the actual parties to this transaction and who paid the gains tax that is the subject of the refund claim, it cannot be concluded that petitioner is even a proper party to this proceeding. Based on the record before us, it appears that a Mr. Philip Pilevsky paid the gains tax due, and it would be Mr. Pilevsky who would have standing to apply for a refund (Tax Law former § 1445[1]; *cf. Matter of Kheel*, Tax Appeals Tribunal, March 1, 1990 [where refund claim made by a corporate officer, on his own behalf, for a refund of penalties paid by corporation was denied]). These are all elements of petitioner's burden to establish it is entitled to a refund. Petitioner has failed to meet that burden (20 NYCRR 3000.15[d][5]; *Matter of Classic Residences*, Tax Appeals Tribunal, December 1, 1994; *Matter of SOGL Assocs.*, Tax Appeals Tribunal, August 4, 1994). In the absence of any evidence to establish that Mr. Pilevsky was acting on behalf of petitioner, 31/32 Lexington Associates is not a proper party and the petition should have been dismissed.

If subject matter jurisdiction was the only issue before us, we would allow the parties additional time to present arguments to us on this issue (*New York State Dept. of Taxation & Fin. v. Tax Appeals Tribunal*, 151 Misc 2d 326, 573 NYS2d 140). However, that is not necessary in this case for even if we decided that we had jurisdiction to entertain the subject mater of petitioner's exception, we conclude that

the Administrative Law Judge properly addressed each of the issues and arguments raised by petitioner, all of which have been dealt with by this Tribunal in prior decisions.

Accordingly, it is ORDERED, ADJUDGED and DECREED that :

1. The exception of 31/32 Lexington Associates is denied;
2. The determination of the Administrative Law Judge is modified; and
3. The petitions of 31/32 Lexington Associates are dismissed.

DATED: Troy, New York
August 21 1997

/s/ Donald C. DeWitt

Donald C. DeWitt
President

/s/ Carroll R. Jenkins

Carroll R. Jenkins
Commissioner

/s/ Joseph W. Pinto, Jr.

Joseph W. Pinto, Jr.
Commissioner

SUPREME COURT OF THE STATE OF NEW YORK
APPELLATE DIVISION: THIRD DEPARTMENT

31/32 LEXINGTON ASSOCIATES,

Petitioner,

- against -

THE TAX APPEALS TRIBUNAL OF THE STATE OF NEW YORK and MICHAEL H. URBACH, COMMISSIONER OF TAXATION AND FINANCE OF THE STATE OF NEW YORK,

Respondents.

VERIFIED PETITION UNDER C.P.L.R. ARTICLE 78

Petitioner, 31/32 Lexington Associates, for its Verified Petition, alleges as follows:

1. Petitioner is a New York general partnership, with its principal place of business at c/o Philips International, 417 Fifth Avenue, New York, New York 10016.

2. Respondent Tax Appeals Tribunal of the State of New York is an agency of the New York State Department of Taxation and Finance.

3. Respondent Michael H. Urbach is Commissioner of Taxation and Finance of the State of New York.

4. Petitioner transferred an interest in 205 and 215 Lexington Avenue, New York, New York (the "Property") to 205-15 Lex Associates ("Buyer") on or about May 26, 1988. No cash was received by Petitioner at the time of the transfer. Petitioner took back Buyer's second mortgage on the Property, as security for Buyer's obligation to pay the purchase price over a five-year period. Pursuant to the applicable provisions of the New York State real property

transfer gains tax, an election was made by Petitioner to pay the gains tax in installments. The scheduled payments of gains tax were made timely by Petitioner. Petitioner had acquired the Property from Lexington Associates ("Original Owner") as a condition to the transfer of the Property by Petitioner to Buyer. Philip Pilevsky, a general partner in Petitioner, acted as nominee for Petitioner in the acquisition of the Property by Petitioner from Original Owner and in the transfer of the Property by Petitioner to Buyer. Copies of Affidavit of David Werner dated March 28, 1996, Transferor Questionnaire dated April 1988, Transferee Questionnaire dated March 22, 1988, Tentative Assessment and Return dated May 26, 1988, Tentative Assessment and Return (Transferee) dated May 26, 1988, and Supplemental Return dated April 26, 1988, are annexed hereto as Exhibits "A," "B," "C," "D," "E," and "F," respectively.

5. The Transferee Questionnaire filed by Philip Pilevsky (as nominee for Petitioner) dated March 22, 1988 reported the anticipated transfer on May 26, 1988 of the Property by Original Owner to Philip Pilevsky for consideration in the amount of $45,100,000. See Exhibit "C."

6. The Transferor Questionnaire filed by Philip Pilevsky (as nominee for Petitioner) dated April 1988 reported the anticipated transfer on May 26, 1988 of the Property by Philip Pilevsky to Buyer for consideration in the amount of $49,100,000. The Transferor Questionnaire reported gain in the amount of $3,915,000 and anticipated gains tax in the amount of $391, 500. See Exhibit "B."

7. The Supplemental Return filed by Philip Pilevsky (as nominee for Petitioner) dated April 26, 1988 reported that no cash was received upon the transfer to Buyer and made the election to pay the entire gains tax of $391,500 in installments. See Exhibit "F."

8. Due to the decline of the real estate market, Buyer was unable to operate the Property profitably after the first three years of ownership. Buyer was unable to keep current

on the first and second mortgages and the other expenses of operating the Property. On or about February 3, 1992, Buyer commenced a Chapter 11 case in the United States Bankruptcy Court for the Southern District of New York, Case No. 92 B 40718 (PBA). Buyer's payments on the second mortgage held by Petitioner ceased upon Buyer's Chapter 11 filing. The filing of the Chapter 11 Petition by Buyer acted as an automatic stay against any attempt by Petitioner to collect further payments. Pursuant to the Plan of Reorganization in Buyer's Bankruptcy case, Petitioner will realize no gain upon the sale of the Property to Buyer. See Exhibit "A." Modified Chapter 11 Plan and Order Confirming Modified Chapter 11 Plan are annexed hereto as Exhibits "G" and "H," respectively.

9. On May 24, 1993, Petitioner timely filed a claim for refund of the first four payments of gains tax (the "First Refund Claim"). A copy of Claim for Refund dated May 24, 1993 (DTA #813845) is annexed hereto as Exhibit "I."

10. On June 7, 1993, the Audit Division wrote to Petitioner's representative for clarification as to the status of Philip Pilevsky as nominee for Petitioner in the subject transaction. A copy of letter dated June 7, 1993 from the Audit Division to Petitioner's representative is annexed hereto as Exhibit "J." On June 24, 1993, Petitioner's representative wrote to the Audit Division to clarify the status of Philip Pilevsky as nominee for Petitioner and enclosed a copy of the Business Certificate for Partners of 31/32 Lexington Associates dated May 26, 1988, signed by Philip Pilevsky, Amram Kass and David Werner as partners. A copy of letter dated June 24, 1993 from Petitioner's representative to the Audit Division is annexed hereto as Exhibit "K." A copy of the Business Certificate of Partners of 31/32 Lexington Associates dated May 26, 1988 is annexed hereto as Exhibit "L." On July 13, 1993, the Audit Division wrote to Petitioner's representative requesting a signed affidavit confirming that Philip Pilevsky was acting as nominee for Petitioner in the subject transaction. A copy of letter dated July 13, 1993 from the Audit Division to

Petitioner's representative is annexed hereto as Exhibit "M." On July 22, 1993, Petitioner's representative wrote to the Audit Division enclosing an affidavit of Philip Pilevsky dated July 16, 1993, confirming that he acted as nominee for the partnership known as 31/32 Lexington Associates in the subject transaction; that the partnership was formed at the time of the transaction, with Philip Pilevsky, Amram Kass and David Werner as partners, and that all real property gains taxes in connection with the transfer were paid by or on behalf of the partnership. A copy of the letter dated July 22, 1993 from Petitioner's representative to the Audit Division, together with a copy of affidavit of Philip Pilevsky dated July 16, 1993, are annexed hereto as Exhibits "N" and "O," respectively.

11. On July 30, 1993, the Audit Division rejected the First Refund Claim. A copy of Refund Denial Letter dated July 30, 1993 (DTA #813845) is annexed hereto as Exhibit "P." On February 17, 1995, the Bureau of Conciliation and Mediation Services ("BCM") issued an order sustaining the Audit Division's rejection of the First Refund Claim. A copy of Conciliation Order dated February 17, 1995 (DTA #813845) is annexed hereto as Exhibit "Q."

12. On May 5, 1995, Petitioner timely filed a petition (DTA No. 813845) with the Division of Tax Appeals, asking for a review of the rejection of the First Refund Claim by the BCM. A copy of Petition dated May 5, 1995 (DTA #813845) is annexed hereto as Exhibit "R."

13. On May 11, 1995, Petitioner timely filed a claim for refund with respect to the fifth (and final) payment of gains tax (the "Second Refund Claim"). A copy of Claim for Refund dated May 11, 1995 (DTA #814194) is annexed hereto as Exhibit "S."

14. On May 24, 1995, the Audit Division denied Petitioner's Second Refund Claim. A copy of Refund Denial letter dated May 24, 1995 (DTA #814194) is annexed hereto as Exhibit "T."

15. On July 26, 1995, the Division of Taxation, in its Answer to the Petition in DTA No. 813845, admitted that Petitioner had paid the gains tax which is the subject of the First Refund Claim but opposed the refund. A copy of Answer with Cover letter dated July 26, 1995 (DTA #813845) is annexed hereto as Exhibit "U."

16. On August 4, 1995, Petitioner timely filed a petition (DTA No. 814194) seeking review of the Audit Division's denial of the Second Refund Claim. A copy of Petition dated August 4, 1995 (DTA #814194) is annexed hereto as Exhibit "V."

17. On October 19, 1995, the Division of Taxation, in its Answer to the Petition in DTA No. 814194, admitted that Petitioner had paid the gains tax which is the subject of the Second Refund Claim but opposed the refund. A copy of Answer with Cover Letter dated October 19, 1995 (DTA #814194) is annexed hereto as Exhibit "W."

18. On July 11, 1996, the Governor signed Chapter 309 of the Laws of 1996, repealing the real property transfer gains tax in its entirety, effective for transfers of real property occurring on or after June 15, 1996.

19. On November 14, 1996, the Administrative Law Judge issued a Determination denying both Petitions and sustaining the Audit Division's denial of both of Petitioner's refund claims. A copy of the determination of the Administrative Law Judge is annexed hereto as Exhibit "X."

20. Thereupon, Petitioner filed with the Tax Appeals Tribunal a timely Notice of Exception to the determination of the Administrative Law Judge. A copy of the Notice of Exception is annexed hereto as Exhibit "Y."

21. On August 21, 1997, Respondent Tax Appeals Tribunal issued a decision, DTA Nos. 813845 and 814194, affirming the determination of the Administrative Law Judge. A copy of the decision of Respondent Tax Appeals Tribunal is annexed hereto as Exhibit "Z."

22. The decision of the Tax Appeals Tribunal was not supported by substantial evidence on the entire record, in that:

(a) Respondent Tax Appeals Tribunal erred in determining that the Division of Taxation, in calculating consideration for gains tax purposes, properly included the face amount of a purchase money second mortgage despite the fact that, due to the bankruptcy of the purchaser, the mortgage was not paid.

(b) Respondent Division of Tax Appeals erred in determining that the imposition of gains tax on the Petitioner, when it has not realized economic gain, does not violate the Petitioner's constitutional right to equal protection of law guaranteed by the Fourteenth Amendment of the United States Constitution and by Article 1, Section 11 of the New York State Constitution.

(c) Respondent Division of Tax Appeals erred in concluding (in *dicta*) that the petition should be dismissed on jurisdictional grounds.

23. Alternatively, the decision of the Tax Appeals Tribunal was affected by an error of law, was arbitrary and capricious, and was an abuse of discretion, in that:

(a) Respondent Tax Appeals Tribunal determined that the Division of Taxation, in calculating consideration for gains tax purposes, properly included the face amount of a purchase money second mortgage despite the fact that, due to the bankruptcy of the purchaser, the mortgage was not paid.

(b) Respondent Division of Tax Appeals determined that the imposition of gains tax on the Petitioner, when it has not realized economic gain, does not violate Petitioner's constitutional right to equal protection of law guaranteed by the Fourteenth Amendment of the United States Constitution and by Article 1, Section 11 of the New York State Constitution.

(c) Respondent Division of Tax Appeals concluded (in *dicta*) that the Petition should be dismissed on jurisdictional grounds.

24. The determination of Respondents Tax Appeals Tribunal and Michael H. Urbach was affected by error of law, was arbitrary and capricious, and was an abuse of discretion.

25. The determination of Respondents Tax Appeals Tribunal and Michael H. Urbach was, on the entire record, not supported by substantial evidence.

26. To the extent that triable issues of fact are raised in this proceeding, Petitioner requests a trial forthwith pursuant to CPLR §7804(h).

WHEREFORE, Petitioner respectfully requests that judgment be entered:

(1) Vacating, annulling and reversing the decision of Respondent Tax Appeals Tribunal dated August 21, 1997:

(2) Granting Petitioner's Claims for Refund of New York State Gains Tax, together with interest thereon; and

(3) Granting Petitioner such other and further relief as the Court finds to be just and proper.

Dated: New York, New York
December 10, 1997

ROBINSON BROG LEINWAND GREENE
GENOVESE & GLUCK P.C.
1345 Avenue of the Americas
New York, New York 10105
Tel: (212) 586-4050
Attorneys for Petitioner
31/32 Lexington Associates

New York State Department of Taxation and Finance

Audit Division

July 30, 1993

31/32 Lex Associates
c/o Philips International
417 Fifth Avenue
New York, NY 10016

Re: Real Property Transfer Gains Tax
Claimant: 31/32 Lex Associates
Property: 205 & 215 Lexington Ave., New York, NY
Case File No.: A-22233-2
Refund No.: R-2211

Gentlemen:

We have considered the above referenced claim for refund dated May 25, 1993, in the amount of $313,200.

The basis of the claim is that as no gain will be realized on the sale of the above property by the claimant, no gains tax is due. Therefore, the $313,200 paid should be refunded to the claimant.

In an attachment to the refund claim, the claimant explained that no cash was received by the claimant on the date of transfer, May 26, 1988. The claimant took back a second mortgage from the purchaser. On or about February 3, 1992, the purchaser commenced a Chapter 11 case, which has stopped the claimant from any further attempts to collect payments due under the mortgage.

Section 1440.1 (a) of Tax Law provides, in part, that "consideration" is "the price paid or *required to be paid* for

real property or any interest therein...." (emphasis added). It also states that consideration includes any price "paid or required to be paid by money, property, or any other thing of value including the amount of any mortgage or purchase money mortgage".

As provided for in Section 1441 and Section 1442. (a) of the Tax Law, the gains tax is computed based on the gain at the *time of transfer*. Also, Section 590.12 of the Gains Tax Regulations states that where a mortgage is given, the consideration would be the *face* amount of the mortgage rather than any future amounts received. In the decision of the Appellate Division of the Supreme Court in *Matter of Cheltoncort Company v. Tax Appeals Tribunal of The State of New York et al.*, the Court affirmed the Tribunal conclusion that, "the value of the consideration has to be determined *at the time of the transfer* in order to finally fix the tax owed. Subsequent events do not alter the value that the consideration had at the time of the transfer" (emphasis added). Section 1445.1 (a) of the Tax Law provides that a refund claim may be filed where the tax was erroneously paid.

In order for the tax to have been "erroneously paid", there must have been some mistake in law or in fact, made at the time the tax was due. A refund would be justified, for example, if the tax had been mistakenly paid on an exempt transfer (a mistake in law) or if the tax was calculated on the wrong amount of consideration (a mistake in fact).

No error was made at the time the tax was due, the date of transfer, because the consideration paid or required to be paid was $4,000,000.

The tax was properly calculated on *the date of transfer*.

Based on all of the above, the refund must be denied in its entirety.

In accordance with Section 1445.2 of the Tax Law, this determination will be final and irrevocable, unless the claimant, within ninety (90) days files either a Request for a Conciliation Conference with the Bureau of Conciliation and Mediation Services or a Petition for a Tax Appeals Hearing with the Division of Tax Appeals. The enclosed form TA-9.1 explains the procedure.

Very truly yours,

Marianne Witkowski
Tax Technician II
Real Property Transfer Gains Tax
Telephone (518) 485-8319

cc: Mr. Babcock MacLean

New York State Department of Taxation and Finance

Audit Division

May 24, 1995

31/32 Lexington Associates
c/o Philips International
417 Fifth Avenue
New York, NY 10016

Re: Real Property Transfer Gains Tax
Claimant: 31/32 Lexington Associates
Property: 205 & 215 Lexington Ave., New York, NY
Case File No.: A-22233-2
Refund No.: R-2211

Gentlemen

We have considered the above referenced claim for refund received May 12, 1995, in the amount of $78,300.

The basis of the claim is that as no gain will be realized on the sale of the above property by the claimant, no gains tax is due. Therefore, the $78,300 paid should be refunded to the claimant.

In an attachment to the refund claim, the claimant explained that no cash was received by the claimant on the date of transfer, May 26, 1988. The claimant took back a second mortgage from the purchaser. On or about February 3, 1992, the purchaser commenced a Chapter 11 case, which has stopped the claimant from any further attempts to collect payments due under the mortgage.

Section 1440.1(a) of the Tax Law provides, in part, that "consideration" is "the price paid or *required to be paid* for

real property or any interest therein..."(emphasis added). It also states that consideration includes any price "paid or required to be paid by money, property, or any other thing of value including the amount of any mortgage or purchase money mortgage".

As provided for in Section 1441 and Section 1442(a) of the Tax Law, the gains tax is computed bases on the gain at the *time of transfer*. Also, Section 590.12 of the Gains Tax Regulations states that where a mortgage is given, the consideration would be the *face* amount of the mortgage rather than any future amounts received. In the decision of the Appellate Division of the Supreme Court in *Matter of Cheltoncort Company v. Tax Appeals Tribunal of The State of New York et al.*, the Court affirmed the Tribunal conclusion that, "the value of the consideration has to be determined *at the time of the transfer* in order to finally fix the tax owed. Subsequent events do not alter the value that the consideration had at the time of the transfer" (emphasis added).

Section 1445.1(a) of the Tax Law provides that a refund claim may be filed where the tax was erroneously paid.

In order for the tax to have been "erroneously paid", there must have been some mistake in law or in fact, made at the time the tax was due. A refund would be justified, for example, if the tax had been mistakenly paid on an exempt transfer (a mistake in law) or if the tax was calculated on the wrong amount of consideration (a mistake in fact).

No error was made at the time the tax was due, the date of transfer, because the consideration paid or required to be paid was $4,000,000. The tax was property calculated on *the date of transfer*.

Based on all of the above, the refund must be denied in its entirety.

In accordance with Section 1445.2 of the Tax Law, this determination shall be final and irrevocable unless claimant within ninety (90) days files either a request for Conciliation Conference with the Bureau of Conciliation and Mediation Services or a Petition for a Tax Appeals Hearing with the Division of Tax Appeals. The enclosed form, TA-9.1, explains this procedure.

Sincerely

Marion V W Kinch
Tax Technician
Real Property Transfer Gains Tax
Telephone (518) 485-8256

Enc.

cc: Mr. Babcock MacLean

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petitions

of

31/32 LEXINGTON ASSOCIATES for Revision of a Determination or for Refund of Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law

DETERMINATION

DTA NOS. 813845 AND 814194

Petitioner, 31/32 Lexington Associates, c/o Philips International, 417 Fifth Avenue, New York, New York 10016, filed petitions for revision of a determination or for refund of tax on gains derived from certain real property transfers under Article 31-B of the Tax Law.

On January 18, 1996 and January 22, 1996, respectively, petitioner by its representative, Babcock MacLean, Esq., and the Division of Taxation by its representative, Steven U. Teitelbaum, Esq. (Herbert M. Friedman, Jr., Esq., of counsel) waived a hearing and agreed to submit this case for determination, with all documents and briefs to be filed by May 27, 1996, which date commenced the six-month period for the issuance of this determination. The Division's documents were submitted on February 23, 1996. Petitioner's documents and brief were received on April 1, 1996. The Division's answering brief and petitioner's reply brief were received on May 2, 1996 and May 28, 1996,[1] respectively.

[1] Petitioner's reply brief was timely filed because it was mailed before the due date.

After due consideration of the entire record, Frank W. Barrie, Administrative Law Judge, renders the following determination.

ISSUE

Whether the Division of Taxation, in calculating consideration for the transfer of a certain interest in real property, properly included the face value of a purchase money mortgage despite its subsequent devaluation, so that the Division's denial of petitioner's refund claims was justified.

FINDINGS OF FACT

1. The record on submission is extremely bare. It does not include a copy of the transferor questionnaire filed by 31/32 Lexington Associates to report its anticipated transfer of the property at issue, 205-215 Lexington Avenue in New York City ("Manhattan property"). Rather, Exhibit "M" of the Division of Taxation ("Division") is a photocopy of a transferee questionnaire filed by Philip Pilevsky, c/o Philips International,[2] dated March 22 1988. Mr. Pilevsky apparently purchased the property at issue from petitioner. This transferee questionnaire reported the anticipated transfer on May 26, 1988 of the Manhattan property by a transferor identified as Lexington Associates, presumably petitioner, 31/32 Lexington Associates, for consideration to be paid by Philip Pilevsky of $45,100,000.00. Mr. Pilevsky reported that the type of interest to be acquired from petitioner in the Manhattan property was (i) a fee interest and (ii) a leasehold assignment or surrender.

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[2] It is observed that petitioner's address shown at the beginning of this determination is also in care of Philips International.

2. The Division's Exhibit "L" is a photocopy of a transferor questionnaire filed by Philip Pilevsky, c/o Philips International, dated April 1988 (without a specific day designated). This transferor questionnaire reported the anticipated transfer on May 26, 1988 of the Manhattan property to a transferee identified as 205-15 Lex Associates. Mr. Pilevsky reported that the type of interest to be transferred in the Manhattan property was a "contract assignment". Consequently, it appears that Mr. Pilevsky flipped his contract to purchase the Manhattan property from petitioner over to an entity known as 205-15 Lex Associates.

3. Petitioner's Exhibit "I" is a short affidavit dated March 28, 1996 of David Werner, who described himself as "a general partner" in petitioner. According to Mr. Werner, petitioner "transferred an interest in 205 and 215 Lexington Avenue . . . to 205-15 Lex Associates . . . on or about May 26, 1988." Mr. Werner provided few details concerning the transaction at issue, and he did not provide any details concerning Mr. Pilevsky's flipping of his apparent contract rights to purchase the property from petitioner to the entity described as 205-15 Lex Associates. It is also unknown if Philip Pilevsky or Philips International also had an ownership interest in petitioner. In brief, the facts concerning the sophisticated and complex real estate transaction at issue are difficult to determine given the limited record on submission.

4. The transferee questionnaire filed by Philip Pilevsky (Division's Exhibit "M") shows consideration to be paid to petitioner by Mr. Pilevsky of $45,100,000.00. In addition, Mr. Pilevsky reported brokerage fees to be paid by him to a real estate broker of $450,000.00. In comparison, the transferor questionnaire filed by Philip Pilevsky (Division's Exhibit "L") shows consideration to be paid to Mr. Pilevsky by 205-15 Lex Associates, c/o Arnold Schotsky, Esq., of the Long Island law firm of Gandin, Schotsky & Rappaport, of $49,100,000.00. Mr. Pilevsky reported a gain subject to tax of $3,915,000.00 after deducting original purchase price of $45,185,000.00 calculated as follows:

Purchase price paid to acquire real property	$45,100,000.00
Legal expenses to acquire property	45,000.00
Legal expenses to sell property	40,000.00
Original purchase price	$45,185,000.00

Consideration to be received from 205-15 Lex Associates of $49,100,000.00 less original purchase price of $45,185,000.00 equals a gain subject to real property transfer gains tax of $3,915,000.00, with anticipated tax due of $391,500.00 (10% of $3,915,000.00).

5. The Division also submitted for review a photocopy of a supplemental return dated April 26, 1988 filed by Mr. Pilevsky as transferor of the property at issue to 205-15 Lex Associates (Division's Exhibit "P"). By this supplemental return, Mr. Pilevsky chose to defer payment of the gains tax due. It appears he elected to pay the tax in equal installments payable on the anniversary date of the transfer for the length of the term of a certain purchase money mortgage, which was apparently used to finance the transaction at issue. However, a copy of the purchase money mortgage was not submitted for review.

6. The Division's "Exhibit D" is a claim for refund of gains tax paid of $313,200.00 dated May 24, 1993, which was filed by David Werner in his capacity of partner of an entity described as "31/21 Lex Associates, a New York partnership". It appears that "Lex" was used erroneously instead of "Lexington" in the description of the entity seeking the refund claim. The petition referred to "31/21 Lexington Associates". This refund claim noted the following minimal facts:

"Seller [presumably petitioner] transferred an interest in [the Manhattan property] to Buyer [presumably Mr. Pilevsky] on or about May 26, 1988.

"No cash was received by Seller at the time of the transfer. Seller took back Buyer's second mortgage on the Property, as security for Buyer's obligation to pay the purchase price over a five-year period. Pursuant to the applicable provisions of the New York State real property gains tax, an election was made by Seller to pay the gains tax in installments. The scheduled payments of gains tax were made timely by Seller."

7. This refund claim dated May 24, 1993 shows tax installments paid on 5/17/89, 5/2/90, 5/20/91 and 5/27/92, which totalled $313,200.00. Petitioner's second refund claim dated May 11, 1995 (Division's Exhibit "I") seeks a refund of a fifth installment payment made on May 26, 1993 of $78,300.00. The two refund claims total $391,500.00, which corresponds to the amount of gains tax reported due by Mr. Pilevsky on his transfer of the Manhattan property to 205-15 Lex Associates. There is nothing in the record to explain why petitioner paid the amount of tax calculated due by Mr. Pilevsky instead of the amount of tax due on its transfer of the Manhattan property to Mr. Pilevsky. Since the consideration to be paid to petitioner by Mr. Pilevsky was approximately $4,000,000.00 less than the consideration Mr. Pilevsky was to receive from 205-15 Lex Associates, as noted in Finding of Fact "4", petitioner's gains tax liability would have been an amount less than $391,500.00. There is no information in the record concerning petitioner's acquisition of the Manhattan property, and its "original purchase price" cannot be determined. Consequently, petitioner's actual gains tax liability on the transfer of the Manhattan property to Mr. Pilevsky is uncertain.

8. Pursuant to an order of the United States Bankruptcy Court dated June 22, 1993 (petitioner's Exhibit "3"), the reorganization of 205-15 Lex Associates under Chapter 11 of the Bankruptcy Code was confirmed. Under the reorganization plan (petitioner's Exhibit "2"), petitioner released and discharged its "Second Mortgagee Claim" against 205-15 Lex Associates in exchange for a payment of $200,000.00. In addition, the Manhattan property was reconveyed to an entity known as 205/215 Lexington Limited Partnership, which apparently was the first mortgagee on the Manhattan property.

9. In its refund claims, petitioner asserts that it "will realize no gain upon the sale of the Property to Buyer" because of the bankruptcy of 205-15 Lex Associates. However, the record does not, in fact, disclose the total payments made by 205-15 Lex Associates to petitioner.

10. By a letter dated July 30, 1993 (Division's Exhibit "E"), petitioner's refund claim dated May 25, 1993 in the amount of $313,200.00 was denied because "[t]he tax was properly calculated on *the date of transfer*" (emphasis in original). By a letter dated May 24, 1995 (Division's Exhibit "J"), petitioner's refund claim dated May 12, 1995 in the amount of $78,300.00 was also denied for the same reason.

SUMMARY OF THE PARTIES' POSITIONS

11. Petitioner argues that denying its refund claims "is contrary to the Tax Law and to basic principles of fairness and common sense" (Petitioner's brief, p. 1). According to petitioner, the gains tax is imposed only on "actual economic gain" (Petitioner's brief, p. 8). It supports this statement by citing to "litigation in the bankruptcy context" where the gains tax has been viewed not as a stamp tax but rather as an income tax, or a tax imposed on economic gain (Petitioner's brief, p. 4). Petitioner also cites to the amendment of the gains tax law in 1993 which deemed "consideration" to be limited to the fair market value of the property transferred to a lender in foreclosure proceedings or a transfer in lieu of foreclosure. Further, petitioner maintains that to "tax a real estate transaction even where gain is *not* derived, would be defective under the Equal Protection Clause" (emphasis in original) (Petitioner's brief, p. 7).

12. The Division counters that in computing consideration the face amount of a mortgage at the time of transfer is properly used, citing the Tax Appeals Tribunal decision in *Matter of Normandy Associates* (March 23, 1989). Subsequent events "which may effect the transferor's actual receipt of [a gain]" are irrelevant (Division's brief, p. 4). The Division also points out that the Tax Appeals Tribunal rejected an equal protection argument, similar to the one made by petitioner, in *Matter of Rapoport* (August 31, 1995).

13. In its reply brief, petitioner maintains that in the cases cited by the Division in its brief, the Tax Appeals Tribunal did not address the situation where "a seller of real property has been taxed on a gain which he did not receive because the purchaser went into bankruptcy" (Petitioner's reply brief, p. 2).

CONCLUSIONS OF LAW

A. Tax Law former § 1441,[3] which became effective March 28, 1983, imposes a 10% tax upon gains derived from the transfer of real property located within New York State.

B. Tax Law former § 1440(3) defined "gain" as the:

> "difference between the consideration for the transfer of real property and the original purchase price of such property, where the consideration exceeds the original purchase price."

Tax Law former § 1440(5)(a)(i) defined "original purchase price" to mean:

> "the consideration paid or required to be paid by the transferor (A) to acquire the interest in real property, and (B) for any capital improvements made or required to be made to such real property. . . ."

"Consideration", in turn, is defined by Tax Law § 1440(l)(a) to mean:

> "the price paid or required to be paid, for real property or any interest therein . . . . Consideration includes any price paid or required to be paid, whether expressed in a deed and whether paid or required to be paid by money, property or any other thing of value and including the amount of any mortgage, purchase money mortgage, lien or encumbrance, whether the underlying indebtedness is assumed or taken subject to."

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[3] The Real Property Transfer Gains Tax imposed by Article 31-B of the Tax Law was repealed on July 13, 1996. The repeal applies to transfers of real property that occur on or after June 15, 1996. *(See*, sections 171 through 180 of chapter 309 of the Laws of 1996.)

C. Petitioner is wrong that gains tax may be imposed only in the case of an actual gain. Rather, gains tax has been imposed in situations of speculative profit and in situations where real estate transactions have soured. In *Matter of Brockman* (Tax Appeals Tribunal, April 4, 1996), arguments similar to those which petitioner has made in this matter were all rejected.

In *Brockman*, the major portion of the sales price was financed by a purchase money note and mortgage from the buyer in the amount of $8,500,000.00. The buyer never made any payments on this note and mortgage, and a foreclosure proceeding was instituted. Like petitioner, the *Brockmans* contended that because they suffered a loss, the imposition of gains tax was not rational and violated their equal protection rights. The Tribunal, in affirming the administrative law judge, denied the Brockmans' claims for refund of gains tax and held them liable for gains tax totalling $193,121.00 on the real estate transaction that had eventually soured.

In its decision in *Brockman*, the Tribunal emphasized that subsequent events do not alter the value that the consideration had at the time of the transfer citing its earlier decision in *Matter of Starburst Dev. Co.* (Tax Appeals Tribunal, May 5, 1994) where the Tribunal stated:

> "the moment that the taxable event occurs, i.e., the transfer of the real property, is the temporal restriction underlying the entire gains tax. Consistent with this interpretation, we have held that the consideration for the transfer is fixed at this moment and is not reduced by subsequent events . . . . To deviate from this theory, as petitioner suggests, and exclude transactions from the definition of transfer of real property based on subsequent events would, in our view, be contrary to the entire scheme of the tax."

The Tribunal in *Brockman* further noted that the Appellate Division had recently sustained its conclusion that the amount of gains tax due is finally determined by the amount of consideration paid or required to be paid on the date of the transfer *(see, Matter of Wanat v. Tax Appeals Tribunal*, ___ AD2d ___, 638 NYS2d 251, *lv denied* ____ NY2d ____, ____ NYS2d ____ [May 7, 1996], *confirming Matter of Wanat*, Tax Appeals Tribunal, September 15, 1994; *Matter of South Suffolk Recreation Ventures v. Tax Appeals Tribunal*, ___ AD2d ___, 638 NYS2d 515, *lv denied* ___ NY2d ___, ___ NYS2d ___ [May 7, 1996], *confirming Matter of South Suffolk Recreation Ventures*, Tax Appeals Tribunal, November 3, 1994). In *Wanat*, which is particularly on point, the Tribunal had decided that the amount of the consideration calculated at the time of the transfer is not affected by the transferee's later default on a note and mortgage.

D. Petitioner's contention that the amendment of the gains tax law in 1993, which deemed "consideration" to be limited to the fair market value of the property transferred to a lender in foreclosure proceedings, means that gains tax may be imposed only on an actual gain is rejected. Laws of 1993 (ch 57, § 60) added a paragraph (d) to the definition of "consideration" at Tax Law § 1440(l) so as to limit "consideration" with respect to a foreclosure transfer (or a deed-in-lieu) to the fair market value of the real property that is transferred. Moreover, this amendment applies to transactions occurring on or after April 15, 1993, pursuant to Laws of 1993 (ch 57, § 418[8]).

E. The Legislature has manifested no intent to ignore a transaction for purposes of gains tax due to subsequent events. Rather, under Tax Law former § 1440(7), the Legislature's definition of "transfer of real property" is extremely broad, and such definition evidences no intent on the part of the Legislature to ignore a transaction as a sale because the sale later turned sour, and the seller failed to profit as planned *(cf., Matter of Shechter*, Tax Appeals Tribunal, October 13, 1994 [wherein the Tribunal noted that

the Legislature evidenced its intent to "look through" an entity to determine the beneficial owners of property by the way it defined "interest in property"]).

F. It is further noted that petitioner is correct that the real property transfer gains tax is not viewed as a stamp tax, but rather as a tax on income in the context of bankruptcy litigation *(see, In re Fifth Avenue Associates, L.P.*, 963 F2d 503, *cert denied* 506 US 947, 121 L Ed 2d 302). Further, such tax is entitled to a priority status under 11 USC § 507(a)(8)(A) as "a tax on or measured by income or gross receipts" (*see*, *In Re Williams*, 173 Bankr 459, *affd* 188 Bankr 331). However, the conclusion that gains tax due is calculated at the time of transfer and may not be reduced by subsequent events does not mean that it is not "a tax on or measured by income or gross receipts" *(see, Matter of Brockman, supra)*.

G. Finally, petitioner's argument that its right to equal protection of the law is violated, by holding it liable for gains tax on a transaction that later soured, is also rejected. The Tribunal addressed this issue in *Matter of Brockman (supra)* as follows:

> "Neither the Federal nor the State constitution require that all taxpayers be treated identically; they only require that those similarly situated be treated uniformly *(see, Matter of Foss v. City of Rochester*, 65 NY2d 247, 491 NYS2d 128; *Matter of Executive Land Corp. v. Chu*, 150 AD2d 7, 545 NYS2d 354). Requiring petitioners to pay the gains tax does not violate their constitutional rights because petitioners are being treated the same as all other similarly situated taxpayers -- they are required to calculate the tax based upon the value of the consideration at the time of the transfer *(see, Matter of Rapoport*, Tax Appeals Tribunal, August 31, 1995)."

H. The petitions of 31/32 Lexington Associates are denied, and the Division of Taxation's denial of petitioner's refund claims is sustained.

DATED: Troy, New York

NOV 14 1996

/s/ Frank W. Barrie

ADMINISTRATIVE LAW JUDGE

STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition

of

31/32 LEXINGTON ASSOCIATES

For Revision of a Determination or for Refund of Tax on Gains Derived from Certain Real Property Transfers under Article 31-B of the Tax Law

Notice of Exception to Administrative Law Judge's Determination

DTA Number 813845 and 814194

Party 31/32 Lexington Associates

Address c/o Philips International, 417 Fifth Avenue, New York, NY 10016

Party's representative, if any Babcock MacLean, Esq.

Telephone No. (212) 603-6315

Address c/o Robinson Brog Leinwand Greene Genovese & Gluck P.C. 1345 Avenue of the Americas, New York, NY 10105

The party named above hereby takes exception to the administrative law judge's determination, pursuant to Section 2006.7 of the Tax Law.

The determination of the administrative law judge was rendered on November 14, 1996.

The party taking exception disagrees with the following findings of fact and conclusions of law of the administrative law judge:

1. The Petitioner disagrees with the conclusion of law of the Administrative Law Judge that the Division of Taxation, in calculating consideration for Gains Tax purposes for the transfer of an interest in real property, properly included the face amount of a purchase money second mortgage despite the fact that the mortgage subsequently became valueless due to the bankruptcy of the purchaser.

2. The Petitioner disagrees with the conclusion of law of the Administrative Law Judge that the imposition of Gains Tax on the Petitioner, when it has not realized any economic gain, does not violate its constitutional rights to equal protection.

The party taking exception requests the following Findings of Facts and Conclusions of Law:

The Petitioner requests the following conclusions of law:

1. The Division of Taxation, in calculating consideration for Gains Tax purposes for the transfer of an interest in real property, improperly included the face amount of a purchase money second mortgage despite the fact that the mortgage subsequently became valueless due to the bankruptcy of the purchaser.

2. The imposition of Gains Tax on the Petitioner, when it has not realized any economic gain, violates its constitutional rights to equal protection.

☒ A brief will be submitted within the 30 day period.

An opportunity for oral argument before the Tribunal is requested ☒ Yes

No other action has been commenced before the Tax Appeals Tribunal nor has the Tribunal previously granted any relief with respect to any of the above-stated items.

Wherefore, the party taking exception requests that the determination of the administrative law judge be reviewed by the Tribunal, and if such determination is found erroneous, that it be reversed or modified.

/s/ Babcock MacLean Attorney	December 9, 1996
Signature of Party or Representative	Date

SUPREME COURT OF THE STATE OF NEW YORK
APPELLATE DIVISION : THIRD DEPARTMENT

31/32 LEXINGTON ASSOCIATES,

Petitioner,

-against-

THE TAX APPEALS TRIBUNAL OF THE STATE OF NEW YORK and MICHAEL H. URBACH, COMMISSIONER OF TAXATION AND FINANCE OF THE STATE OF NEW YORK,

Respondents.

No. 81231

STIPULATION

WHEREAS Petitioner has brought this proceeding under Article 78 of the Civil Practice Law and Rules to review a determination of the New York Tax Appeals Tribunal dated August 21, 1997 (the "Decision"); and

WHEREAS in the Decision, there was discussion by the Tax Appeals Tribunal concerning whether Petitioner was a proper party to bring the petition before the Tax Appeals Tribunal, and thus whether the petition before the Tax Appeals Tribunal should have been dismissed on jurisdictional grounds (*see, e.g.*, the Decision at pp. 11 – 12); and

WHEREAS at the time this matter was before the Audit Division of the Department of Taxation and Finance, the Audit Division raised with counsel for Petitioner the question of whether Petitioner was the Transferror and was the proper party, and Petitioner provided to the Audit Division certain documents, including those documents annexed as Exhibits "J" through "O" to the Petition in this proceeding; and

WHEREAS Respondent Commissioner through the Division of Taxation, by its attorneys, stated in its Answers before the Division of Tax Appeals that "Petitioner [31/32 Lexington Associates] transferred the real property located at 205 and 215 Lexington Avenue, New York City" and that "Petitioner took a mortgage on the property from the purchaser" (*see* Answers of Division of Taxation before the Division of Tax Appeals at ¶ 2) and that "the gains tax was paid by Petitioner, but it subsequently filed a Claim for Refund. . . ." (*see id.*, ¶ 5); and

WHEREAS the parties agreed that the identity of the Transferror, and Petitioner's standing, are not issues in this case, and therefore Petitioner did not introduce evidence regarding its standing as the proper party to the proceedings below, but would have been prepared to offer those documents annexed to the Petition herein as Exhibits "J" through "O" on that issue;

NOW, THEREFORE the parties by their attorneys hereby stipulate and agree as follows:

1. Respondent hereby withdraws the denial set forth in paragraph FOURTH of Respondent's Answer herein.

2. Respondent hereby withdraws the denial set forth in paragraph FIFTH of Respondent's Answer herein regarding whether Philip Pilevsky filed a supplemental return as the nominee for Petitioner.

3. The parties stipulate that Petitioner is the proper party in interest in this proceeding.

4. Petitioner withdraws Exhibits "J" through "O" from the Petition.

Dated: Albany, New York
March 23, 1998

ROBINSON BROG LEINWAND
GREENE GENOVESE & GLUCK, P.C.

/s/

by: Babcock MacLean
1345 Avenue of the Americas
New York, New York 10105
212-586-4050
Attorneys for Petitioner

Dated: March 30, 1998

DENNIS C. VACCO
Attorney General of the
State of New York

/s/

by: Julie S. Mereson,
Assistant Attorney General
The Capitol
Albany, New York 12224
518-474-3654
Attorneys for Respondents